

"Value and the Legal Stuff"

Presented by:

Bill Gilliland
June 19, 2014

Dentons' Global Offices



Legend
Offices, associate offices* and facilities*
Associate firms and special alliances*

North America Energy Corridor

- Edmonton
- Calgary
- Dallas
- Houston

3

DENTONS

Outline

Value

- | | |
|----------------------------------|----|
| • Letter of Intent | \$ |
| • Due Diligence Preparedness | \$ |
| • Representations and Warranties | \$ |
| • Indemnification Provisions | \$ |
| • Material Adverse Change | \$ |
| • Working Capital Adjustment | \$ |
| • Holdback/Escrow | \$ |
| • Earnouts | \$ |

4

DENTONS

Due Diligence Preparedness

- Value/risk assessment
- Eliminate Risks
- Clarify Risks

5

DENTONS

Representations and Warranties

- Determined by what can and cannot be said in the circumstances

OR

- "Risk allocation" mechanism
- "Joint and several" vs. "several"
- Support value assumptions
- Support value drivers
- Qualifiers – potential "value retention" – knowledge, materiality

6

DENTONS

Indemnification Provisions

- Thresholds
 - individual claims
 - aggregate claims
- Deductibles
- Caps
- Risks impact indemnity limitations

7

DENTONS

Indemnification Provisions

- "No claims may be asserted by the Purchaser or the Purchaser's Representatives under indemnity unless and until the aggregate of the Losses of the Purchaser and its Representatives collectively, in respect of such Claims exceeds <> Dollars (\$<>) in the aggregate, in which event the amount of all such Loss including such <> Dollar (\$<>) amount may be asserted."
- Does each individual claim need to exceed a specified threshold?
- Potential "value retention"

8

DENTONS

Indemnity Caps

- Limit on claims
- Trend towards less than purchase price
- Significant percentage of deals significantly less than 50% of purchase price

9

DENTONS

Material Adverse Change Conditions

- No Material Adverse Change in respect of PCo shall have occurred after the date hereof and prior to the Effective Date

10

DENTONS

Material Adverse Change Conditions

"Material Adverse Change" or "Material Adverse Effect" means, with respect to any Person, any fact or state of facts, circumstance, change, effect, occurrence or event which:

(a) either individually is or in the aggregate are, or individually or in the aggregate would reasonably be expected to be, material and adverse to the business, operations, results of operations, properties, assets, liabilities, obligations (whether absolute, accrued, conditional or otherwise) or condition (financial or otherwise) of such Person and its Subsidiaries, on a consolidated basis, except to the extent of any fact or state of facts, circumstance, change, effect, occurrence or event resulting from or arising in connection with:

(i) any change in Canadian GAAP or changes in regulatory accounting requirements applicable to the oil and gas, oil sands and oil shale exploration, development and production businesses, the petrochemicals industry, and the business of refining, marketing and distributing petroleum products (the "O&G Business");

(ii) any change in global, national or regional political conditions (including the outbreak of war or acts of terrorism) or in general economic, business, regulatory, or market conditions or in national or global financial or capital markets;

(iii) any change generally affecting the O&G Business;

(iv) any natural disaster;

(v) any decline in crude oil or natural gas prices on a current or forward basis;

(vi) any actions taken (or omitted by to be taken) at the written request of other Party hereto; or

(vii) any action taken by the Person or any of its Subsidiaries that is required pursuant to this Agreement (excluding any obligation to act in the ordinary course of business, but including any steps taken pursuant to Section 5.3(a) to obtain any required regulatory approvals),

provided, however, that with respect to clauses (i), (ii), (iii) and (iv) such matter does not have a materially disproportionate effect on the Person and its Subsidiaries, taken as a whole, relative to comparable entities operating in the O&G Business, and references in certain sections of this Agreement to dollar amounts are not intended to be, and shall not be deemed to be, illustrative or interpretative for purposes of determining whether a "Material Adverse Change" or a "Material Adverse Effect" has occurred; or

(b) either individually or in the aggregate prevents, or individually or in aggregate would reasonably be expected to prevent, the Person from performing its material obligations under this Agreement in any material respect;

Three Elements:

- General definition of what it is
- Exceptions – matters with respect to which parties assume the risk and impact on value
- Limitations on the exceptions

Working Capital Adjustments

- "Your watch/My watch"
- Capturing pre-closing results of business
- Financial Statements
- Need accounting advice
- Buyer traditionally prepares post-closing calculations
- Seller should be comfortable with methodology specified in Agreement

13

DENTONS

Hold Back/Escrow of Purchase Price

- Considerations
- Exclusive remedy? - rare
- Amount of escrow - significant majority of deals less than 10% of purchase price
- For what? - indemnity claims and/or purchase price adjustments
- Consider R&W Insurance as alternative

14

DENTONS

Earnouts

- An earnout is a risk-allocation mechanism used in an acquisition transaction where a portion of the purchase price is deferred and is calculated based on the performance of the acquired business over a specified time period following the closing
- Increasingly used in transactions

15

DENTONS

Why an Earnout?

- Valuation Gap
- Financing
- Incentive-Based Compensation
- Startups/Early Stage

16

DENTONS

Earnouts - Items to Consider

- Defining the business that will "earn out"
 - existing/expansions
 - integration
- The performance measure
 - revenue
 - net income
 - EBITDA
 - non-financial
- The accounting standard
 - accounting principles
 - practices
 - assumptions
 - inter-company/non-recurring

17

DENTONS

Earnouts - Items to Consider

- The payout timing and the earnout period
 - instalments / %
 - caps
 - "all or nothing"
- Post-closing control and support of the "earning out business"
 - approval rights/ restrictive covenants
 - affirmative support/level of efforts
- Tax considerations

18

DENTONS

Questions and Answers

Bill Gilliland

bill.gilliland@dentons.com
403.268.6826